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October 30, 2013

VIA ELECTRONIC MAIL

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Securities and Exchange Commission
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Attn.: Elizabeth M. Murphy, Secretary

Board of Governors of the
Federal Reserve System
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Washington, DC 20551
Attn: Robert deV. Frierson, Secretary

Federal Housing Finance Agency
Eighth Floor
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Attn.: Alfred M. Pollard, General Counsel

Federal Deposit Insurance Corporation
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Washington, DC 20429
Attn.: Comments, Robert E. Feldman,
Executive Secretary

Department of Housing and
Urban Development
Regulations Division
Office of General Counsel
451 7th Street, SW, Room 10276
Washington, DC 20410-0500

**Re: Comments on Credit Risk Retention Provisions of the Dodd-Frank Wall Street Reform
and Consumer Protection Act of 2010 Relating to CLOs**

**SEC (Release No. 34-64603; File No. S7-14-11); FDIC (RIN 3064-AD74); OCC (Docket
Number OCC-2013-0010); FRB (Docket No. R-1411); FHFA (RIN 2590-AA43); HUD (RIN
2501-AD53)**

Ladies and Gentlemen:

Thank you for the opportunity to submit comments to the joint notice of proposed rulemaking (the “**Proposing Release**”) issued by your agencies (the “**Agencies**”) on August 28, 2013, relating to credit risk retention as mandated by Section 15G of the Securities Exchange Act

of 1934 (as amended, the “**Exchange Act**”), added pursuant to Section 941(b) of the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “**Dodd-Frank Act**”).¹

Symphony Asset Management

We are Symphony Asset Management LLC (“**Symphony**”), a diversified investment manager headquartered in San Francisco, CA with an office in New York, NY. Founded in 1994, our firm currently employs 76 professionals and manages \$13.9 billion in assets. Symphony manages investments across a variety of funds, including managed collateralized loan obligation funds (“**CLOs**”). As of September 30, 2013, Symphony managed \$4.7 billion of CLOs, including leverage. The firm managed an additional \$5.4 billion in long-only loans through various account structures including closed-end funds, open-end funds and institutional mandates. In addition to managing CLOs and other loan funds, we also invest as an investment manager on behalf of our clients in the equity and in most classes of debt of other third-party managed CLOs.

Symphony has performed among the top ranked managers of CLOs. We have received awards for outstanding CLO management.² It is important to note that some CLOs, including Symphony’s,³ have increased the overcollateralization coverage ratios,⁴ a measure of credit quality, even after giving effect to cash distributions. Improvements in the overcollateralization coverage ratios, in the case of Symphony’s CLOs, come from active portfolio management.

Overview

Symphony believes that the Dodd-Frank Act did not intend to cover CLOs and that the inclusion of CLOs within the risk retention regime is based upon two key misconceptions. The first misconception is that a CLO is part of an originate-to-distribute model. A CLO is not an originate-to-distribute asset; it is an actively managed investment in corporate bank loans. The second misconception is that a CLO is the same, or even similar to, a CDO; other than similarities in name and legal structure, a CLO is not a CDO.

We have been closely following the Agencies’ risk retention proposals as applied to CLOs since the initial 2011 release. Following our review of the Proposing Release and the Agencies’ discussion of CLOs therein, we felt it was important to highlight the fact that CDOs and CLOs are very distinct products, despite the similar treatment they receive under the

¹ Dodd-Frank Wall Street Reform and Consumer Protection Act, Pub. L. No. 111-203, 124 Stat. 1376 (2010).

² Symphony, in its role as investment manager, has been nominated for awards by and has received awards from CreditFlux, a leading publication in the CLO industry. For example, in 2011, Symphony CLO II won Best 2006 U.S. CLO and was nominated for the Best CLO Manager, Best Recent CLO (Symphony CLO VI) and Best 2005 US CLO (Symphony CLO I). (Note, awards are issued at the maturity of the transaction, not the issuance date). In 2013, Symphony CLO V won Best Seasoned US CLO.

³ This information is as of September 30, 2013 and includes Symphony CLOs I through V and Symphony CLOs VII through XI. Symphony CLO VI is no longer outstanding, and Symphony CLO XII closed in October.

⁴ An overcollateralization ratio is defined specifically for each CLO, but is roughly represented by the aggregate par amount of assets divided by the aggregate par amount of rated liabilities.

Proposing Release. It is with this goal in mind that we, with the assistance of outside counsel, are submitting our comments on the Proposing Release with a specific focus on distinguishing CLOs from other products subject to risk retention.

Our letter sets forth our analysis of the Proposing Release and Section 15G of the Exchange Act and our respectful disagreement with the Agencies' interpretation of the statute. We believe that a key difference between CLOs and CDOs is the asset-by-asset credit process⁵ – a process nearly impossible to mimic in any re-securitization – and that active portfolio management based upon that process distinguishes a CLO investment manager from a sponsor of other re-securitizations, including CDOs. While there is no common definition of a “CDO”, we use the term here to focus on those transactions (including “CDOs squared”) mentioned in the legislative history of the Dodd-Frank Act – namely those consisting of securitizations of other asset backed securities. Typically, those securitizations (1) could have exposure to thousands of illiquid credits, compared to 100 to 200 of liquid credits in a typical CLO and (2) for a variety of reasons, do not allow for credit analysis of the underlying borrowers supporting the securitization or re-securitization. We are grateful for the opportunity to submit this letter to you.

CLO Investment Managers are Not the Sponsor of CLOs

As an initial matter, we acknowledge the daunting task assigned to the Agencies by Congress and the myriad of assets securitized. Our belief is that CDOs and CLOs are extremely different financial structures, although one may not view them as such due to similarities in their names and legal structures. As an investment manager who, pre-credit crisis, declined to manage re-securitization vehicles, we have explored the differences between a CLO and a re-securitization from a credit perspective. This analysis, together with discussions with our legal counsel and our collective research have led us to a divergent view of both the plain language of the statute as it applies to CLOs, as well as the Congressional intent regarding CLOs and risk retention, than the application the Agencies have set forth in the Proposing Release.

1. Background

In the 2011 version of the proposed rules to implement risk retention as mandated by Section 15G of the Exchange Act (the “**Initial Proposed Rules**”), the Agencies included a footnote indicating that a CLO investment manager “generally” acts as the sponsor of a CLO “by selecting the commercial loans to be purchased by an agent bank for inclusion in the CLO collateral pool, and then manages the securitized assets once deposited in the CLO structure.”⁶ In the Proposing Release, the Agencies responded to commenters that questioned the Agencies' inclusion of CLO investment managers in the definition of sponsor by explaining that, in the

⁵ The investment process typically includes analysis aimed at obtaining a rigorous understanding and knowledge of underlying industries and companies for each investment. The investment process incorporates a fundamental overview as well as a credit view of a company or business by one of Symphony's industry analysts. These analysts typically formulate their views of the investment/loan based upon their opinions of a variety of factors including the company, related industries, collateral packages and the credit agreement. Symphony monitors each investment using a rigorous process that factors in economic conditions, market views, technical issues and individual fundamental company views.

⁶ 76 Fed. Reg. 83 (the “**Initial Proposed Rules**”) at 30 n. 42.

view of the Agencies, a CLO investment manager is a “securitizer” because it “typically organizes and initiates the transaction as it has control over the formation of the CLO collateral pool” and it also “indirectly transfers the underlying assets to the CLO issuing entity typically by selecting the assets and directing the CLO issuing entity to purchase and sell those assets.”⁷

We disagree with the Agencies’ interpretation of the definition of “securitizer” as applied to a CLO investment manager on the basis that the inclusion of a CLO investment manager is simply not within the plain meaning of the language in the Exchange Act. Congress appears to have spoken very specifically on the point and, even if the text of the Exchange Act is ambiguous, the legislative history does not support a conclusion that Congress sought to treat a CLO investment manager as the sponsor of a CLO.

Additionally, following our discussions with counsel, we have found no evidence that Congress had securitizations of liquid, broadly syndicated loans (including CLOs) in mind when crafting the risk retention provisions of the Dodd-Frank Act. As a result, both the Initial Proposed Rules and the Proposing Release have struggled to reconcile the statute with a real world application to CLOs and demonstrate a lack of recognition of the differences between a CLO and other products like CDOs which arise out of the originate-to-distribute model.

The legislative history and the language of the statute support the conclusion that Congress intended to regulate sponsors of CDO transactions, which were extensions of the originate-to-distribute model for mortgage finance. Our market experience is that CDOs had a different genesis than CLOs. The underlying assets of CDOs were generated in the Congressionally-identified originate-to-distribute model and were not nearly as liquid as the loans that collateralize CLOs. A CDOs’ assets were likely sourced from one or two structurers of the CDO without any market check (i.e., trading) on the creditworthiness of those assets. The initial sponsors of those transactions were easily identifiable. However, the liquid nature of a CLO asset pool means that the highly tradable assets were not tied to a select group of originators but were instead simply selected by the CLO investment manager based on their creditworthiness and price in the open market. CLO investors, including the CLO investment manager, have clear visibility to the underlying quality of the assets.

In our experience, the level of transparency surrounding a CLO is significantly better than any re-securitization vehicle. As an initial matter, the underlying loans included in CLOs are typically made to companies who (1) have audited and unaudited financial statements available, (2) often file periodic reports with the Securities Exchange Commission, (3) are subject to rigorous diligence by law firms and investment banks at the time of loan origination, (4) are reviewed by numerous market participants who purchase portions of the loans, (5) may have research published by independent third-party sources about them and (6) often have their own websites describing their business and their products. A CLO will often make available monthly, and in many cases on a website available to investors, the names of each borrower whose loan is included in the CLO, allowing investors to perform a loan-by-loan analysis of a CLO. In addition, loan pricing services often publish data and provide daily market prices for

⁷ Proposing Release at 144-145.

each loan, thereby providing more clarity around others' views of the relative creditworthiness of the borrower.

2. *Applicability of the Chevron Test*

When discussing the plain language of the statute and whether it applies to CLOs with counsel, we were introduced to the Chevron⁸ Test. Based on our understanding of the test, we do not believe that the Agencies promulgation of the Proposed Rules meets the prongs set forth by the Supreme Court. The Supreme Court, in its *Chevron* decision, set forth the standard for review of an agency's promulgation of formal rules. The first prong of the analysis is "whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear . . . the agency, must give effect to the unambiguously expressed intent of Congress."⁹ Moving on from the first prong of the analysis, "if the statute is silent or ambiguous with respect to the specific issue, the question for the court is whether the agency's answer is based on a permissible construction of the statute."¹⁰

Prong 1: Interpreting the Plain Meaning of the Statute

"Securitizer" is defined under the Exchange Act as "(A) an issuer of an asset-backed security or (B) a person who organizes and initiates an asset-backed securities transaction by selling or transferring assets, either directly or indirectly, including through an affiliate, to the issuer."¹¹ The Agencies have referred to part (B) of this definition as a "sponsor" and proposed that risk retention be held by the sponsor of an asset-backed securities transaction.

The plain meaning of the definition indicates that to be a sponsor, and therefore to be subject to the requirement to retain credit risk, a party to a securitization must both (1) organize and initiate an asset-backed securities transaction and (2) do so by selling or transferring assets to the issuer (whether directly or indirectly). Therefore, steps taken to organize and initiate an asset-backed securities transaction do not make a party a securitizer unless such steps include the sale or transfer of assets to the issuer. Yet, in the Proposing Release, the Agencies state that a CLO investment manager organizes and initiates the transaction because it "has control over the formation of the CLO collateral pool" and a CLO investment manager transfers the underlying assets to the CLO issuing entity indirectly "typically by selecting the assets and directing the CLO issuing entity to purchase and sell those assets."¹² We fail to see how having control over the formation of the collateral pool and selecting the assets included in the collateral pool are distinct actions that could satisfy the two distinct requirements of the definition of sponsor. This is especially notable when considering the ordinary meaning and purpose at the heart of the statute: retaining exposure to assets that one has an incentive to originate and distribute. Critically, even if having the ability to affect the composition of the collateral pool could satisfy

⁸ *Chevron U.S.A. Inc. v. Natural Resources Def. Council, Inc.*, 467 U.S. 837 (1984) ("*Chevron*").

⁹ *Chevron* at 843-844.

¹⁰ *Chevron* at 844.

¹¹ Exchange Act, Section 15G(a)(3).

¹² Proposing Release at 143-144.

the first requirement of the definition, we do not believe it satisfies the second requirement of transferring assets to the CLO entity.

In our role as CLO investment manager, the issuing entity contractually engages us to manage its portfolio of assets. The contract pursuant to which this engagement is set forth is described in an offering circular that is reviewed and commented on by investors. Similarly, the specific parameters of the portfolio, with which we must comply to purchase assets, is set forth in the offering circular and subject to investor review and comment. We then select loans for the CLO to purchase from market participants, and negotiate the amount of a loan to be purchased as well as the purchase price for the loan. However, at no point do we, the investment manager, own the loans. Each loan is sourced from third parties and transferred by such third party to the issuer and, therefore, we cannot sell or otherwise transfer the loans to the issuer. We do not believe that selecting assets¹³ for the CLO constitutes indirectly transferring those assets for the simple reason that the actual (direct or indirect) owners of the assets must agree to sell and relinquish all economic ownership those assets to the CLO once we have selected them. Instead, we believe an indirect transfer is one in which an economically interested *owner* of an asset, through a subsidiary or other intermediary, transfers that asset to the ultimate recipient.¹⁴

Prong 2: Determination of Deference to the Agencies

As discussed above, we do not believe the definition of sponsor is ambiguous. In the context of a CLO, a CLO investment manager does not satisfy the requirements of the definition of a sponsor because it does not transfer assets either directly or indirectly to the CLO. However, given the scope of the Dodd-Frank Act, we have also considered whether Congress was inadvertently silent on the sponsor for a CLO transaction, thus allowing the Agencies to fill an interpretive gap. In such a case, the *Chevron* analysis requires a court to consider whether an agency's interpretation of the statute is reasonable.¹⁵ In this instance, the question is whether the Agencies' interpretation of the word "transfer" is reasonable. The Agencies have recognized the possibility that their interpretation may be questioned and have leaned on the intent of Congress for support, noting that "Congress intended for risk retention to be held by collateral asset managers (such as CLO or CDO managers), who are the parties who determine the credit risk profile of securitized assets in many types of securitization transactions . . ."¹⁶ We do not believe Congress had the same intent for CDOs and investment funds managing liquid assets.

The legislative history of Section 941 of the Dodd-Frank Act is not extensive. The primary piece is the Senate Committee on Banking, Housing, and Urban Development's Report

¹³ We note that the Dodd-Frank Act does not mention "selection of the assets." In addition, if an asset owner does not agree to sell an asset that a CLO manager selects, there would be no statutorily required "transfer".

¹⁴ The statutory language specifies that the sale or transfer of assets "through an affiliate" would be an indirect transfer. The inclusion of sales by affiliates in the definition's language is the only example of an indirect transfer expressly stated and provides insight as to the type of transaction meant to be covered. In other words, the use of the word "indirectly" in the definition does not alter the requirement that the asset be transferred by its owner (i.e. someone who has an economic interest that is being relinquished); rather it permits the transfer to occur in one or more steps.

¹⁵ *Chevron* at 843-844.

¹⁶ Proposing Release at 144.

on the Dodd-Frank Restoring American Financial Stability Act of 2010, S. REP. NO. 111-176 (the “Senate Report”), which includes a section-by-section analysis of the Dodd-Frank Act and cites nine authorities in Section 941’s legislative history. Six of the authorities were testimony before the committee and three were written reports.

The Senate Report’s discussion of Section 941(b) (i) identifies the problems leading to the financial crisis that the section is meant to address, (ii) states the section’s general purpose, and (iii) describes how the Senate majority expects the section to operate, including with respect to the Agencies writing regulations under it. As explained in the Senate Report, Congress designed the risk retention regime to address two specific problems that contributed to the financial crisis of 2008.

The first problem identified by Congress was the originate-to-distribute model of extending credit, where “loans were made expressly to be sold into securitization pools, which meant that the lenders did not expect to bear the credit risk of borrower default.” It follows that risk retention targeted vehicles that were used for capital generation for originators (in order to continue to extend credit to collect fees) rather than as true investment opportunities for investors. Consequently, Section 941 places a risk retention requirement on securitizers with the goal of aligning their economic interests with those of investors in asset-backed securities. Section 941 is also intended to raise credit and underwriting standards by placing originators “under increasing market discipline because securitizers who retain risk will be unwilling to purchase poor-quality assets.”

The second problem Congress sought to address with the risk retention requirement was also related to the originate to distribute model: the lack of transparency for investors in asset-backed securities with respect to the underlying obligations. The Senate Report states that “[c]omplexity and opacity in securitization markets created the conditions that allowed the financial shock from the subprime mortgage sector to spread into a global financial crisis . . .” In residential mortgage-backed securities transactions and CDOs that re-securitized residential mortgage-backed securities, investors did not have visibility to the creditworthiness of the obligors whose payments the lenders depended on for the repayment of the asset-backed securities.

We do not believe that assigning the risk retention requirement to CLO investment managers addresses Congress’s goals because a CLO’s assets are liquid and transparent, and the proposed securitizer/sponsor of a CLO has little or no influence in the origination process. As to whether underwriting standards can be improved by requiring CLO investment managers to retain the mandatory risk retention, we note that we select loans based upon our credit analysis and our assessment of relative value of the assets to be purchased by the CLOs that we manage in the secondary market. Furthermore, the compensation structure in the CLOs we manage already aligns our interests with those of our investors. Very simply, requiring us to hold a risk retention position will not contribute to the accomplishment of Congress’ goals.

As to the second problem identified by Congress, we note that the collateral for CLO transactions consists exclusively of corporate credits.¹⁷ Perhaps 100-200 loans comprise the total collateral for a CLO transaction, and those same loans may be held across several of the CLO funds managed by the CLO investment manager. The loan obligors are known entities on which investors and the CLO investment manager can perform extensive diligence. Such loans trade on an individual basis and we are able to trade at the appropriate market value for a loan based upon our assessment of the credit risk of the obligor. This is in stark contrast to residential mortgage-backed securities transactions where the collateral pool consists of thousands of residential mortgages, identifiable to investors only by characteristics, not individual names. It is therefore not possible to perform credit analysis on individual obligors in such transactions or trade away such low quality loans on an individual basis. Accordingly, the transparency problem identified by Congress is not present in CLOs and mandating risk retention on CLO investment managers will not address this goal.

After examining the legislative history, we believe that neither CLOs nor their investment advisers are the intended targets of the risk retention regime and that the Agencies' interpretation of the definition of sponsor to include CLO investment managers is not a permissible one. The Senate Report specifically states that the "implementation of risk retention obligations should recognize the differences in securitization practices for various asset classes" and the statute provides the Agencies with the flexibility to adopt exemptions, exceptions or adjustments to the standard risk retention requirement. We encourage the Agencies to consider alternative approaches to risk retention for CLOs, including an exemption for the most liquid underlying assets or a retention regime of one in which independent third-parties that specifically negotiate for an eligible horizontal residual interest be allowed to hold the required risk retention.

We greatly appreciate your consideration of the views set forth in this letter, and we would be pleased to have the opportunity to discuss these matters further with you or with any member of the staff of any of the Agencies. Please feel free to contact Judith MacDonald at judith.macdonald@symphonyasset.com.

Very truly yours,



Gunther Stein
Chief Investment Officer and CEO
Symphony Asset Management LLC

¹⁷ Typically, the investment parameters for a CLO require a minimum of 90% of the portfolio be invested in senior secured bank loans, with the remaining 10% consisting of other bank loans and corporate bonds.